No. 15,541

IN THE

United States Court of Appeals

For the Ninth Circuit

BANK OF NEVADA,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

On Appeal from the Judgment of the United States District Court for the District of Nevada.

BRIEF FOR THE APPELLEE.

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Index

Citations

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OPINION BELOW.

The opinion, findings of fact and conclusions of law of the District Court (R. 32-43) are not officially reported.

JURISDICTION.

This appeal (R. 45) involves the application of the penalty provided in Section 6332 of the Internal Revenue Code of 1954 for the failure to surrender property subject to a levy. On June 10, 1955, the District Director of Internal Revenue served a notice

of levy upon the Bank of Nevada, in the amount o $1,069.70, for income and excise taxes assessed agains one J. D. Bentley. (R. 41-42; Ex. F, R. 28.) On Jun 14, 1955, the District Director served a final deman upon the Bank of Nevada. (R. 43; Ex. H, R. 30.) O September 28, 1955, the United States filed a com plaint in the United States District Court for th District of Nevada, praying for judgment against th Bank of Nevada in the sum of $878.16 together wit interest as allowed by law. (R. 3-5.) On November 1955, the Bank of Nevada filed an answer to this com plaint. (R. 6-8.) Jurisdiction was conferred on th District Court by 28 U.S.C., Sections 1340 and/o 1345. On March 29, 1957, the District Court enterd judgment in favor of the United States. (R. 44.) Th case is brought to this Court by a notice of appel filed April 5, 1957. (R. 45.) Jurisdiction is conferrd on this Court by 28 U.S.C., Section 1291.

QUESTION PRESENTED.

Whether the District Court was correct in conclu- ing that federal tax liens against a delinquent ta- payer's bank account were paramount and vad against an alleged right of set-off against the accout asserted by the bank and that the bank, therefore, ws in possession of property subject to a levy and ws liable for the failure to surrender such property.

STATUTES INVOLVED.

The pertinent provisions of the Internal Revenue Codes of 1939 and 1954 are set forth in the Appendix, *infra.*

STATEMENT.

The facts as found by the District Court (R. 40-43) are entirely stipulated (R. 9-31) and may be summarized as follows:

On November 15, 1954, certain withholding and Federal Insurance Contribution Act taxes for the calendar year 1954 in the amount of $804.50 were assessed against J. D. Bentley (hereinafter called taxpayer), of Las Vegas, Nevada. On November 16, 1954, taxpayer was notified of this assessment and demand was made upon him to pay it, but he refused to do so. On January 12, 1955, a notice of tax lien pertaining to this assessment of Withholding and Federal Insurance Contribution Act taxes was filed in the Office of the County Recorder, Clark County, Nevada. (R. 10, 40-41; Ex. A, R. 14.)

On February 28, 1955, the taxpayer submitted a financial statement to the Bank of Nevada (hereinafter called the Bank), which is a corporation organized and existing under the laws of the State of Nevada, with its principal place of business in Las Vegas, Clark County, Nevada. (R. 10, 40-41.) In part, this financial statement (Ex. B, R. 15-16) stated (R. 15):

The undersigned, for the purpose of procurin and establishing credit from time to time with yo and to induce you to permit the undersigned t become indebted to you on notes, endorsement guarantees, overdrafts or otherwise, furnishes th following as being a true and correct statemei of the financial condition of the undersigned o the above date, and agrees to notify you immed ately of the extent and character of any materi change in said financial condition, and also agre that if the undersigned, or any endorser or gua antor of any of the obligations of the undersigne, at any time fails in business or becomes insolver, or commits an act of bankruptcy, or if any depos account of the undersigned with you, or any oth property of the undersigned held by you, be a tempted to be obtained or held by writ of exec tion, garnishment, attachment or other legl process, or if any of the representations mae below prove to be untrue, or if the undersignd fails to notify you of any material change s above agreed, then and in such case, at yor option, all of the obligations of the undersignd to you, or held by you, shall immediately becoe due and payable, without demand or notice. Ths statement shall be construed by you to be a co tinuing statement of the condition of the und signed, and a new and original statement of ll assets and liabilities upon each and every tra action in and by which the undersigned hereaf r becomes indebted to you, until the undersigd advises in writing to the contrary.

Earlier, on August 31, 1954, the taxpayer had s mitted a financial statement on the same form. (R. 0, 41; Ex. B-1, R. 17-18.)

On March 1, 1955, certain federal excise taxes for he calendar year 1954 in the amount of $187.51 were ssessed against the taxpayer and, on that same date, he taxpayer was notified of this assessment and de- nand was made upon him to pay it, but he refused o do so. (R. 11, 41.)

On April 16, 1955, taxpayer and his wife borrowed 2,000 from the Bank and executed a promissory note n favor of the Bank for that amount. (R. 11, 41; Ex. C, R. 19.)

On May 31, 1955, the taxpayer submitted another nancial statement to the Bank. (R. 11, 41; Ex. D, . 20-21.)

On June 10, 1955, the taxpayer had on deposit in n account with the Bank the sum of not less than 378.16. On that day, the District Director of Internal evenue, through H. L. Collomb, collection officer, rved a notice of levy, Form 668-A, upon the Bank delivering it to E. K. Phillips, assistant cashier, at :45 P.M. This notice of levy covered both of the ssessments, together with statutory additions thereto. R. 11-12, 41-42; Exs. E and F, R. 22-27, 28.)

On that same day, A. M. Smith, vice-president and anager of the First and Fremont Branch of the ank, wrote to H. L. Collomb, collection officer, as llows (R. 12, 42):

> This will acknowledge receipt of your Notice of Levy against J. D. Bentley, which was served on our Mr. Phillips at 1:45 p.m. today.
>
> I would like to take this opportunity to inform you that we have exercised our right to set-off and

> applied the funds in this account to an unsecure indebtedness held at this bank; consequently there are no funds available under your levy.

The "unsecured indebtedness" referred to in th letter was the balance of the note referred to abov which, at the time of the levy, amounted to approx mately $1,500. The Bank, subsequent to 1:45 p.m. o June 10, 1955, exercised its claimed right of set-off an applied the funds in the bank account to the ta payer's unsecured indebtedness. (R. 12, 31, 42.)[1]

On June 13, 1955, a notice of federal tax lien pe taining to the assessment of the federal excise taxe was filed in the Office of the County Recorder, Cla County, Nevada. On June 14, 1955, the District Dire tor of Internal Revenue, through H. L. Collomb, c lection officer, served a final demand, Form 668-, upon the Bank by delivering it to A. M. Smith, vi president and manager of the First and Fremo Branch of the Bank at 11:10 a.m. (R. 12-13, 43; Es. G and H, R. 29, 30.)

On September 28, 1955, the United States brought the instant suit for collection. (R. 3-5.) On March 4, 1957, the District Court concluded, on the basis of he foregoing facts, that the tax liens were paramount and valid (R. 43) and, on March 29, 1957, the court entered judgment in favor of the United States in the amount

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[1]The bank statements of the checking account in question, maintained in the name of Bentley's Trading Post, indicate that there were substantial deposits and withdrawals for several months after the claimed right of set-off and that the Bank accepted these deposits and honored these withdrawls. (Ex. E, R. 22-27.)

f $878.16, together with interest thereon (R. 44), whereupon the Bank brought this appeal. (R. 45.)

SUMMARY OF ARGUMENT.

Sections 6321, 6322, 6331 and 6332 of the Internal Revenue Code of 1954 provide that if any person liable to pay any tax neglects or refuses to pay the tax after demand, the amount of the tax becomes a lien in favor of the United States upon all property, whether real or personal; this lien arises at the time the tax is assessed and continues until the liability for the amount assessed is satisfied. If the taxpayer neglects or refuses to pay the tax after notice and demand is made upon him, the Government may levy upon all property and rights to property belonging to the taxpayer or on which there is a lien. The person who is in possession of property which is subject to levy shall, upon demand, surrender such property to the Government and, if such persons fails or refuses to do so, he is liable in his own person or estate to the United States in a sum equal to the value of the property (not to exceed the amount of the taxes for the collection for which the levy has been made).

It is well-established that a bank account is "property or rights to property" within the meaning of the foregoing statutory provisions. And it is clear from the facts of this case that, on June 10, 1955, the Bank of Nevada was in possession of a bank account belonging to the delinquent taxpayer upon which tax liens had attached on November 15, 1954, and March 1, 1955,

and which was therefore subject to levy. Demand wa properly made upon the Bank on June 10, 1955, an the Bank refused to surrender the account, thereb becoming personally liable in a sum equal to th amount of the account, which did not exceed th amount of the taxes for which the levy was made.

The Bank contends, however, that it was not i possession of property of the taxpayer which wa subject to levy at the time the levy and demand wer made. This contention is based on the assertion tha the Bank had a contractual right of set-off by virtu of an agreement set forth in a financial statement su- mitted to the Bank by the taxpayer on August 3, 1954, and an equitable right of set-off by virtue of promissory note which was executed by the taxpaye on April 16, 1955, and that these rights of set-off wer paramount to the Government's lien. The Bank tho argues that, since the allegedly paramount right f set-off was greater than the bank account, there wa no property of the taxpayer in its possession. Ths contention and the underlying assertions upon whi it is based are not supported by the facts of this cae or the law with respect thereto; the Bank could nt immunize the account from the federal tax levy by a inchoate agreement with its depositor nor by n asserted equitable right of set-off arising from a det which was not in existence at the time the tax lies arose.

The contractual right of set-off was clearly inchoate at all material times. The agreement amounted o nothing more than a potential right to set-off in fe

vent the taxpayer became indebted to the Bank and ne of several contingencies set forth in the agreement ccurred and the Bank exercised its option to set-off. he debt which the Bank is attempting to set off, ursuant to the agreement, did not even arise until fter the tax liens attached. Furthermore, the only ontingency which occurred to give the Bank its con- actual option to set-off was the levy and demand and ie option, accordingly, did not arise, and was not xercised, until *after* levy and demand. Indeed, it is ot even clear that the Bank in fact exercised its ption to set-off. The Bank is endeavoring to relate ie asserted exercise of its contractual option to set- f back to the date of the original, inchoate financial tatement, but the doctrine of relation-back cannot perate to preclude the Government from its right to wy on the bank account of the delinquent taxpayer, rticularly where, as here, the debt arose after the x liens attached and the option to set-off arose, and s exercise occurred, not only after the liens attached, it after the demand was made upon the Bank.

It is equally clear that the promissory note did not ve rise to any equitable right of set-off which would feat the Government's levy. Whether the note is emed to be a demand note which was due on the te of its execution (April 16, 1955), as the Bank serts, or whether the note was not due until August , 1955, in absence of a demand, as the District Court ld, any equitable right of levy arose after the tax ns attached and such right was necessarily born th the liens impressed thereon. Furthermore, it does

not appear that such equitable right exists at all o the facts of this case. The mere fact that a note i due does not give rise to an equitable right of set-off such right does not exist in absence of facts whic show that the maker cannot or will not pay or tha the creditor has no practical legal remedy.

It might also be noted that the Bank's attempt t assert a right of set-off is tantamount to an assertio by the Bank of a prior lien. However, even if th question is viewed as one involving the priority o liens, it is clear that the tax liens were paramour. Accordingly, the Government's levy was valid and th Bank was required to surrender the bank account o be liable for its failure to do so. The cases upon whic the Bank relies are distinguishable or inapplicab. Similarly, the Bank's closing argument that a decisio against it infringes upon normal banking transactio's and impairs the making of bank loans is withot merit. The priority of the tax liens, the statutory rigt of levy, and the statutory liability of the Bank fr failure to surrender the bank account are clear. Thee is nothing in the statute or decisions to indicate tht banks are to be placed in any special position or ae to be accorded any preferred treatment as compard with other types of creditors.

The decision of the District Court is correct ad should be affirmed.

ARGUMENT.

THE DISTRICT COURT CORRECTLY HELD THAT CERTAIN FEDERAL TAX LIENS WERE PARAMOUNT AND THAT THE BANK WAS LIABLE FOR FAILING TO SURRENDER, AFTER LEVY AND DEMAND, A BANK ACCOUNT TO WHICH THE LIENS HAD ATTACHED.

The lien for federal taxes, and the provisions for the collection thereof, are entirely statutory and their scope and effect are to be determined solely by the statute and the decisions interpreting them. See *MacKenzie v. United States,* 109 F. 2d 540, 541 (C.A. 9th). The statute provides that, if any person liable to pay any tax neglects or refuses to pay the tax after demand, the amount of the tax becomes a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person. Sec. 6321 of the Internal Revenue Code of 1954 (Appendix, *infra.*) This lien is deemed to arise at the time the assessment is made and continues until the liability for the amount assessed is satisfied. Sec. 6322 of the Internal Revenue Code of 1954 (Appendix, *infra*). If the person who is liable to pay the tax neglects or refuses to do so within ten days after notice and demand is made upon him, the Secretary of the Treasury) or his delegate, may collect such tax by levy upon all property and rights to property (with certain exceptions not pertinent here) belonging to such person or on which there is a lien. Sec. 6331 of the Internal Revenue Code of 1954 (Appendix, *infra.*) Upon such a levy, any person who is in possession of property or rights to property which are subject to the levy shall, upon demand, surrender such property or rights to the Secretary or his dele-

gate, unless the property is, at the time of demand subject to an attachment or execution under any judicial process. Any person who, upon demand, fails or refuses to surrender property or rights to property which is subject to levy is liable in his own person or estate to the United States in a sum equal to the value of the property not surrendered (not to exceed the amount of the taxes for the collection of which the levy has been made, together with costs and statutory interest from the date of the levy). Sec. 6332(a) and (b) of the Internal Revenue Code of 1954 (Appendix *infra.*) It is a well-established principle, which taxpayer does not dispute (Br. 7), that the word "property", as used in the statutory provisions set forth above, has a very broad meaning and includes obligations, debts owing to the taxpayer, and other intangibles, and that a bank account, being a debt of the bank to the depositor, is "property and rights to property" against which a lien may attach and a levy may be made under the statutes here involved. *United States v. Liverpool & London Ins. Co.,* 348 U.S. 21; *United States v. Eiland,* 223 F. 2d 118 (C.A. 4th); *United States v. Manufacturers Trust Co.,* 198 F. 2d 366 (C.A. 2d); *United States v. Long Island Drug Co.,* 115 F. 2d 983 (C.A. 2d); *MacKenzie v. United States, supra.* See also *Glass City Bank v. United States,* 326 U.S. 265. It is clear that the Bank was in possession of property belonging to a delinquent taxpayer and upon which a tax lien had attached and that this property was subject to levy. Demand was properly made upon the Bank and the Bank refused

o surrender the property. The Bank, pursuant to he foregoing statutory authority, was, accordingly, ersonally liable for its failure to surrender such roperty.

Specifically, on November 15, 1954, taxes in the mount of $804.50 were assessed against the taxpayer; he taxpayer was notified of this assessment and de- nand was made upon him to pay it, but he neglected r refused to do so. (R. 10, 40-41.) Later, on March , 1955, additional taxes in the amount of $187.51 ere assessed against the taxpayer, notice was served, nd demand was made upon him; the taxpayer also eglected or refused to pay these taxes. (R. 11, 41.) lore than ten days having passed from the time of ese notices and demands, the District Director was uthorized to levy upon all property or rights to roperty belonging to the taxpayer or on which there as a federal tax lien with respect to the taxes which ere the subject of the notices and demands. Sec. 31(a) of the Internal Revenue Code of 1954. On ne 10, 1955, the taxpayer had on deposit in a check- g account with the Bank the sum of not less than 78.16. (R. 11, 41.) This checking account, under e authorities cited above, was clearly "property" or ights to property" of the taxpayer; it was also roperty on which there was a federal tax lien, such ens arising on November 15, 1954 (in the amount $804.50), and on March 1, 1955 (in the amount $187.51), the dates of the assessments. Secs. 6321 nd 6322 of the Internal Revenue Code of 1954. On ne 10, 1955, the District Director properly levied

upon this account and demanded the surrender thereo by the Bank. (R. 11-12, 41-42.) The Bank was re quired by statute to surrender this account. Sec 6332(a) of the Internal Revenue Code of 1954. Th Bank refused to surrender the account (R. 12, 42 and, on June 14, 1955, the District Director made final demand on the Bank (R. 12-13, 43), which sti refuses to surrender it. The Bank has thus becom liable in its own person and estate to the Unite States in the sum equal to the amount of the accou ($878.16), which amount does not exceed the amou of the taxes for which the levy was made. ($992.01. The Bank is also liable for costs and six per cent pe annum interest on the amount of the levy from th date thereof, June 10, 1955. Sec. 6332(b) of the In ternal Revenue Code of 1954. *United States v. Wasi ington Trust Co. of Pittsburgh, Pa.* (W.D. Pa., decided April 13, 1956 (56-2 U.S.T.C., par. 9603); *United States v. Peoples State Bank* (S.D. Ind., decided August 17, 1955 (55-2 U.S.T.C., par. 9655.

The terms of Section 6332(a) of the 1954 Coe permit the Bank only two defenses: (1) that it wa not in possession of property of the taxpayer whic was subject to levy, or (2) that the property wa subject to a prior judicial attachment or executio. The statute admits of no other defenses. *United State v. Manufacturers Trust Co., supra; Commonweal Bank v. United States,* 115 2d 327 (C.A. 6th); *Unit States v. Third Nat. Bank & Trust Co.,* 111 F. Sup. 152 (M.D. Pa.). Here, there is no question of a ju cial attachment or execution by the Bank or anyo

se. The Bank does contend, however (Br. 8, 11), at it was not in possession of property of the tax-ayer which was subject to levy at the time of demand nd levy. This contention is based on the assertion Br. 8, 11) that the Bank had a contractual right of t-off by virtue of the agreement set forth in the nancial statement submitted to the Bank by the xpayer on August 31, 1954, and an equitable right set-off by virtue of the promissory note executed taxpayer on April 16, 1955. The Bank then submits Br. 12-13) that these rights of set-off were para-ount to the Government's tax lien. Since the al-gedly paramount set-off was greater than the de-sit, there was, the Bank argues, no property of the xpayer in its possession. This contention and the derlying assertions upon which it is based are not pported by the facts of this case or the law with spect thereto. The Bank could not immunize the count from the federal tax levy by an inchoate reement with its depositor nor by an asserted uitable right of set-off arising from a debt which as not in existence at the time the tax liens arose. *nited States v. Manufacturers Trust Co., supra,* p. 9; *United States v. Graham,* 96 F. Supp. 318 (S.D. l.), affirmed *per curiam sub nom. State of Califor-a v. United States,* 195 F. 2d 530 (C.A. 9th); cf. *nited States v. Security Tr. & Sav. Bk.,* 340 U.S. , 50-51; *United States v. Kings County Iron Works,* 4 F. 2d 232, 236 (C.A. 2d).

With respect to the asserted right of set-off result-g from the agreement set forth in the financial state-

ment of August 31, 1954, the Bank is attempting t defeat the federal tax levy by means of a contractu right which was clearly inchoate at all material time. The agreement amounted to nothing more than a potential right to set-off in the event (1) the taxpaye became indebted to the Bank, (2) one of severl contingencies occurred, and (3) the Bank exercisd its option to set-off. (R. 15.) The record does nt show that taxpayer was even indebted to the Ban at or about the time the agreement was executed. Th debt which the Bank is attempting to set off dl not even arise until April 16, 1955 (R. 22), almosta year after the agreement was executed and after te tax liens arose (the taxes being assessed on Novembr 15, 1954, and March 1, 1955 (R. 10, 11, 40-41)). As to the contingencies which were set forth in the agre- ment before the Bank could exercise its option o set-off, these were, specifically, if taxpayer becare insolvent, failed in business, or committed an act f bankruptcy; or if the deposit account or any othr property of taxpayer held by the Bank was the su- ject of an attempt to be obtained by execution, ga- nishment, attachment or other legal process; or f any of the representations made by taxpayer provd to be untrue; or if taxpayer failed to notify the Bak of any material change in financial condition. (R. 15. Here, there is no question of insolvency, business fa- ure, acts of bankruptcy or misrepresentation by ta- payer. Similarly, there is no proof that taxpaye's financial condition materially changed—the mere fat that taxpayer refused to pay the tax and the Gover-

ent levied on his bank account does not mean that e did not have other assets to pay the tax or the debt that his financial condition changed. The only fact hich gave the Bank the option to set-off was the overnment's demand and levy—which occurred *prior* the asserted exercise of the option.

Finally, it does not even clearly appear that the ank actually exercised its option to set-off. Although e Bank stated in a letter to the collection officer R. 12, 42) that it was exercising its option to set-off, e bank records show that it did not in fact set off e amount in taxpayer's bank account against the bt owed the Bank, but instead, honored taxpayers thdrawals on the date of the set-off and charged xpayer's account with the amount of the Govern-ent levy, not the amount of the remaining balance the account ($209.71, plus a $20 deposit which was cepted) or the amount of the debt owing to the nk ($1,500). Indeed, the Bank continued to honor thdrawals and accept deposits thereafter and it does t appear that it ever set off the full amount of the bt. (R. 26-27.) The Bank is endeavoring to relate asserted exercise of its contractual option to set-back to the date of the original, inchoate financial tement which taxpayer submitted to the Bank on gust 31, 1954.[2] As the foregoing facts clearly show, e debt arose after the tax liens attached and the eged exercise of the option occurred not only after

[2] Taxpayer executed similar financial statements on February 28, 5 (R. 15-16), and on May 31, 1955 (R. 20-21), but does not con-d that these agreements are involved.

the liens attached, but after the demand was made upon the Bank. The doctrine of relation-back cannot operate to destroy the realities of this situation and cannot preclude the Government from pursuing its right to levy on the bank account of the delinquent taxpayer. See *United States v. Security Tr. & Sv. Bk., supra,* p. 50.

It is equally clear that the assertion (Br. 8, 11) that the promissory note executed on April 16, 1955, gave rise to an equitable right of set-off which defeated the Government's levy is without merit. Taxpayer's contention in this respect is predicated on the assertion (Br. 8-10) that the note was a demand note and was therefore due on the date of its execution and delivery. Assuming, *arguendo,* that this is true, it only means that if an equitable right of set-off existed in favor of the Bank as a result of the note, it arose no earlier than April 16, 1955 (the date the note was executed), which was *after* the tax liens in question attached. Such right necessarily was born with the federal tax liens impressed thereon. *United States v. Graham, supra.* Moreover, the District Court found (R. 36, 40) that it was *not* the intention of the parties that the note was to be due immediately upon delivery, but that the note in question had not matured and was not intended to be payable prior to August 14, 1955, in absence of a demand. The court properly recognized that the rule that a note payable on demand is deemed to be due immediately does not apply where there is something on the paper or in the circumstances to show the contrary. *Sullivan v.*

llis, 219 Fed. 694, 696 (C.A. 8th). Here, the face
t the note,[3] together with the fact that even when
e set-off was asserted on June 10, 1955, the Bank
d not set off the entire amount due on the note
$1,500), supports the District Court's finding that
e note was not intended to be due until August
, 1955, unless demand was made sooner. Under this
ternative view of the facts, the note was not due
ntil after the tax liens attached and the demand and
vy were made upon the Bank and any equitable right
set-off based upon the note, if such right existed
all, did not arise until then. Under either view of
e facts, the Bank's asserted equitable right of set-
(based upon the note) cannot defeat the levy.
urthermore, the mere fact that the note might be
e, regardless of the date, does not mean that an
uitable right of set-off exists. Such right would not
ist in the absence of facts which show that the
aker cannot pay (as where the maker becomes in-
lvent), or will not do so (as where the maker
fuses to pay upon demand after maturity), or
here the creditor has no practical legal remedy.
nerican Surety Co. v. City of Akron, 95 F. 2d 966
.A. 6th); see, *J. L. Hudson Co. v. Thomas,* 6 F.
pp. 857 (E.D. Mich.).

It might also be noted that the Bank's attempt to
sert a right of set-off is tantamount to an assertion

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[3] The note read, in part, as follows (R. 35):

On Demand; if no demand is made then on August 14th, 1955, for value received, I promise to pay in lawful money of the United States of America, to the order of the Bank of Nevada * * * Two Thousand and no/100 Dollars.

by the Bank of a prior lien. Indeed, in its brief n the District Court, the Bank expressly contended (t. 36) that the right of set-off created a lien on the bak deposits which was prior to the federal tax liens ad, in this Court, the Bank likewise contends (Br. 12-1) that its right of set-off is paramount to the tax lies. Technically, the instant suit is one to enforce te liability for failure to surrender property which is subject to a levy, as provided by Section 6332(b) of the 1954 Code and is not a suit to directly assert a prior lien. Cf. *Commonwealth Bank v. United Stats, supra; United States v. Third Nat. Bank & Trust C., supra.* The question of the priority of the tax lins which are involved here arrises indirectly from ne Bank's efforts to show that it did not hold propety subject to levy, but that an allegedly prior right of set-off existed which extinguished the taxpaye's property rights prior to the attachment of the ax liens or the date of the levy. However, even if ne question is viewed solely as one involving the priority of liens, it is clear that the tax liens in question wre paramount to any rights of the Bank and it follows, *a fortiori,* that the Government's levy was valid ad that the Bank was required to surrender the propety or be liable for its failure to do so.

As fully discussed in connection with the queston of whether the Bank held property subject to ley, the priority of liens depends upon the time the len attaches and becomes choate, and the priority o a federal tax lien is not defeated by a contingent, n-choate lien. A lien is inchoate, in the federal sese,

henever numerous contingencies might arise before
ie lien ripens and is only perfected when there is
bthing more to be done to have a choate lien. *United*
tates v. New Britain, 347 U.S. 81; *United States v.*
cri, 348 U.S. 211; *United States v. Liverpool & Lon-*
n Ins. Co., supra; United States v. Security Tr. &
w. Bk., supra. As discussed above, the agreement
l the financial statement of August 14, 1954, and any
n which might arise therefrom, were clearly inchoate
the time of the agreement's execution and at the
ne the tax liens arose (November 15, 1954, and
arch 1, 1955), and at the time of the levy and de-
and (June 10, 1955). There was no certainty on
igust 14, 1955, that a loan would be made by the
nk and, after a loan was made on April 16, 1955,
ere was no certainty that any of the contingencies
t forth in the agreement would arise or that the
nk would exercise its option to set-off even if one
the contingencies did occur. Indeed, it was only
e very levy and demand in question which provided
e occurrence which occasioned the Bank to exercise
option to set-off, and, clearly, it was not until
ter this levy that the Bank expressed its desire to
ercise its option. Even then, as noted above, it is
t clear that the Bank actually did set off the debt.

Insofar as any lien arising from the note is con-
ned, it is apparent that the note, being executed
er the tax liens arose, was subordinate thereto. The
nk, as the creditor on a note, was clearly not a
rtgagee, pledgee, purchaser or judgment creditor
ich would be entitled to priority under Section

6323 of the Internal Revenue Code of 1954 (Appendix, *infra*). See *United States v. Security Tr. & Sav. Bk., supra,* pp. 51-53.[4]

Thus, whether the question be viewed as one involving the question of whether the Bank held property of a delinquent taxpayer which was subject to levy (and thus was under an obligation to surrender such property upon levy and demand or be subject to a statutory penalty), or as a question involving the priority of liens, the District Court was correct in concluding (R.43) that the Government's liens were paramount and valid and that the Government was entitled to judgment.

Taxpayer relies upon *United States v. Winnett,* 165 F. 2d 149 (C.A. 9th) (Br. 7, 12), but, as was noted by the District Court in *United States v. Graham, supra,* the facts in the *Winnett* case are clearly distinguishable from those in the case at bar. In the *Winnett* case, the underlying debt owing from the delinquent taxpayer to Winnett was in existence, and the taxpayer was found to be insolvent prior to the attachment of the tax liens. This Court held, in the *Winnett* case (p. 151), that the right of setoff accrued because of (and on the date of) the taxpayer's insolvency. Here, as discussed above, the underlying debt owing from the delinquent taxpayer to

[4]In addition to the Bank not being one of the four classes of parties against whom the tax lien is invalid unless first recorded, the first lien in question (which arose on November 15, 1954) was recorded on January 12, 1955, before the note in question was executed. (R. 10, 41.)

e Bank (the note) did not exist until after the tax ns arose; there was and is no insolvency involved; d there are no other facts giving rise to a right of t-off until after the liens attached. Taxpayer also es the *Winnett* case (Br. 11) as holding that the llector can reach nothing that the taxpayer could t have reached. Assuming, *arguendo,* that this oposition is correct, we would like to point out that e taxpayer, *at the time of the levy and demand,* d full right to use his bank account and, indeed, the day of the levy, taxpayer withdrew and de- sited various amounts and has continued to do so. R. 26-27.) The Bank did not, in fact, attempt to s off any portion of the debt until after the demand s made upon it. (R. 12, 31, 42.) In connection h the statement in the *Winnett* case (p. 151) that e equitable right of set-off relates back to the date the agreement, no only did the Court later refuse apply the doctrine of relation-back in a case in ich the right of set-off accrued subsequent to the liens (*United States v. Graham, supra*) but it uld be noted that the *Winnett* case was decided or to *United States v. Security Tr. & Sav. Bk., ora,* in which the Supreme Court (340 U.S., p. 50) d that the doctrine of relation-back could not be plied to defeat a federal tax lien. Finally, it is now ar that the inequity which disturbed this Court the *Winnett* case, i.e., the possibility that Winnett uld be required to pay the debt being levied upon ce (i.e., to the Government and to his creditor) s not exist. In the event the person levied upon is

required to turn over the property involved or to p.y the penalty upon refusal to do so, that person woul be released from further liability to the extent of ls payments. *United States v. Eiland, supra; Unitd States v. Manufacturers Trust Co., supra; Unitd States v. Peoples State Bank, supra.* Indeed, nt only does the *Graham* case assist in distinguishing te *Winnett* case, but it lends direct support to the Ge- ernment's position. In the *Graham* case, the Unitd States sought to enforce tax liens against amous earned by the taxpayer under leases with the Stre of California. The federal liens preceded the accrul of any amounts to the taxpayer under the leases. Tie State refused to honor the federal liens, asserting tht it was entitled to set off the taxpayer's unpaid stte taxes against the amounts later accrued on the leass. In an action to foreclose on the liens, the Distict Court held that the State's right of set-off, if sch existed, was secondary to the federal tax lien, statig (96 F. Supp., p. 321):

> The 1942 income tax assessment against ne taxpayer, Warren C. Graham, was received by the Collector on March 23, 1945, more thai a year and three months before the leases with he State of California were entered into. The ax due under this assessment is still due. Any mo'ey that accrued to the taxpayer under the lease vth the state accrued with a lien impressed uponit. There was no period of time in which the Sate of California's right of set-off could have bei asserted against the debt to the taxpayer that he property was not impressed with the tax lien.In

U.S. v. Winnett, supra, the right of set-off accrued before any tax liens arose.

* * * * * * *

Assuming arguendo that the State of California may assert an equitable set-off against a delinquent taxpayer, the set-off could have been asserted no earlier than the time at which the lease agreements were entered into with the taxpayer. No set-off could arise until such time as there existed something to be set-off against. But the rights of the taxpayer under the lease were born with the tax lien impressed thereon.

Assuming further that the set-off and the tax liens attached simultaneously to the interest of the taxpayer created by the lease agreements, no citation of authority is needed to establish that the federal tax lien is superior to any simultaneously attaching interest of the State of California. Therefore, the rights of the defendant, State of California, with respect to the money accrued as rentals under the leases made with the taxpayer are inferior to the tax liens of the United States.

axpayer also relies upon *Updike v. Manufacturers ust Co.,* 243 App. Div. 15, 275 N.Y.S. 716. (Br. 7, 13.) This case deals with the right of a bank, ler New York law, to set off a depositor's unmaed note against a deposit, upon notice of a material nge in the depositor's financial condition and does deal with the priority of tax liens or the extent the Government's right to levy against a creditor a delinquent taxpayer who also holds property

of the taxpayer. The latter issue, which is the qu involved here, is a federal question and is to be de termined by federal law. State law, particularly th of New York (when the case involves a Nevada ban taxpayer and transaction), should not control. S *United States v. Scovil,* 348 U.S. 218, 220; *United States v. Acri,* 348 U.S. 211, 213; *United States v. Security Tr. & Sav. Bk., supra,* p. 49.

In conclusion, the Bank's closing argument (pp. 13) that the decision of the District Court infringes upon the rights of a bank and its depositor to enter into usual banking transactions and will impair the making of bank loans is not material to the issues in this case. The priority of the tax liens as set by statute and judicial decisions, the broad statutory remedy of levy as a device to enforce the collection of taxes (see *United States v. Eiland, supra,* pp. 121-122; *United States v. Manufacturers Trust Co., supra* p. 368), and the personal liability of the Bank for failure to surrender property levied upon are clear. There is nothing in the statute or the decisions to indicate that banks are to be placed in any special position or are to be accorded any preferred treatment as compared with other types of creditors.

CONCLUSION.

The decision of the District Court is correct and ould be affirmed.

Respectfully submitted,

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September, 1957.

(Appendix Follows.)

Appendix.

Internal Revenue Code of 1954:

C. 6321. LIEN FOR TAXES.

If any person liable to pay any tax neglects or uses to pay the same after demand, the amount cluding any interest, additional amount, additional tax, or assessable penalty, together with any costs t may accrue in addition thereto) shall be a lien favor of the United States upon all property and hts to property, whether real or personal, belonging such person.

U.S.C. 1952 ed., Supp. II, Sec. 6321.)

C. 6322. PERIOD OF LIEN.

Unless another date is specifically fixed by law, the n imposed by section 6321 shall arise at the time assessment is made and shall continue until the bility for the amount so assessed is satisfied or be- es unenforceable by reason of lapse of time.

U.S.C. 1952 ed., Supp. II, Sec. 6322.)

C. 6323. VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS.

a) *Invalidity of Lien Without Notice.*—Except otherwise provided in subsection (c), the lien imed by section 6321 shall not be valid as against mortgagee, pledgee, purchaser, or judgment credi- until notice thereof has been filed by the Secretary is delegate—

(1) *Under state or territorial laws.*—In the office designated by the law of the State or Territory in which the property subject to the lien

is situated, whenever the State or Territory as by law designated an office within the State or Territory for the filing of such notice; or

* * *

(26 U.S.C. 1952 ed., Supp. II, Sec. 6323.)

SEC. 6331. LEVY AND DISTRAINT.

(a) *Authority of Secretary or Delegate.*—If ny person liable to pay any tax neglects or refuses to pay the same within 10 days after notice and demand, it shall be lawful for the Secretary or his delegate to collect such tax (and such further sum as shall be sufficient to cover the expenses of the levy) by levy upon all property and rights to property (except such property as is exempt under section 6334) belonging to such person or on which there is a lien provided in this chapter for the payment of such tax.

* * *

(b) *Seizure and Sale of Property.*—The term "levy" as used in this title includes the power of distraint and seizure by any means. In any case in which the Secretary of his delegate may levy upon property or rights to property, he may seize and sell such property or rights to property (whether real or personal, tangible or intangible).

* * *

(26 U.S.C. 1952 ed., Supp. II, Sec. 6331.)

SEC. 6332. SURRENDER OF PROPERTY SUBJECT TO LEVY.

(a) *Requirement.*—Any person in possession of (or obligated with respect to) property or rights to

property subject to levy upon which a levy has been made shall, upon demand of the Secretary or his delegate, surrender such property or rights (or discharge such obligation) to the Secretary or his delegate, except such part of the property or rights as is at the time of such demand, subject to an attachment or execution under any judicial process.

(b) *Penalty for Violation.*—Any person who fails or refuses to surrender as required by subsection (a) any property or rights to property, subject to levy, upon demand by the Secretary or his delegate, shall be liable in his own person and estate to the United States in a sum equal to the value of the property or rights not so surrendered, but not exceeding the amount of the taxes for the collection of which such levy has been made, together with costs and interest on such sum at the rate of 6 percent per annum from the date of such levy.

* * *

(26 U.S.C. 1952 ed., Supp. II, Sec. 6332.)

The provisions of Sections 3670, 3671, 3672, 3690 and 3710 of the Internal Revenue Code of 1939 are substantially the same as the provisions of the 1954 Code which are set forth above. The above provisions of the 1954 Code are applicable after January 1, 1955, to all internal revenue taxes whether imposed by the 1939 or 1954 Codes. Section 7851(a)(6)(B) of the Internal Revenue Code of 1954 (26 U.S.C. 1952 ed., Supp. II, Sec. 7851.)